REPORT OF EXAMINATION
OF THE

CSE SAFEGUARD INSURANCE COMPANY

AS OF
DECEMBER 31, 2006

Participating State
and Zone:

California

Filed May 20, 2008

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San Francisco, California
April 25, 2008

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition (EX4) Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable Kent Michie
Secretary, Zone IV-Western
Commissioner of Insurance
Department of Insurance, State of Utah
Salt Lake City, Utah

Honorable Steve Poizner
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Secretary, and Commissioner:

Pursuant to your instructions, an examination was made of the

CSE SAFEGUARD INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 50 California Street, Suite 2550, San Francisco, California 94111.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2002. This examination covers the period from January 1, 2003 through December 31, 2006. The examination was conducted pursuant to the National Association of Insurance Commissioners' (NAIC) plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions, and an evaluation of assets and a determination of liabilities as of December 31, 2006, as deemed necessary under the circumstances. The examination was conducted concurrently with that of the Company's immediate parent, Civil Service Employees Insurance Company.

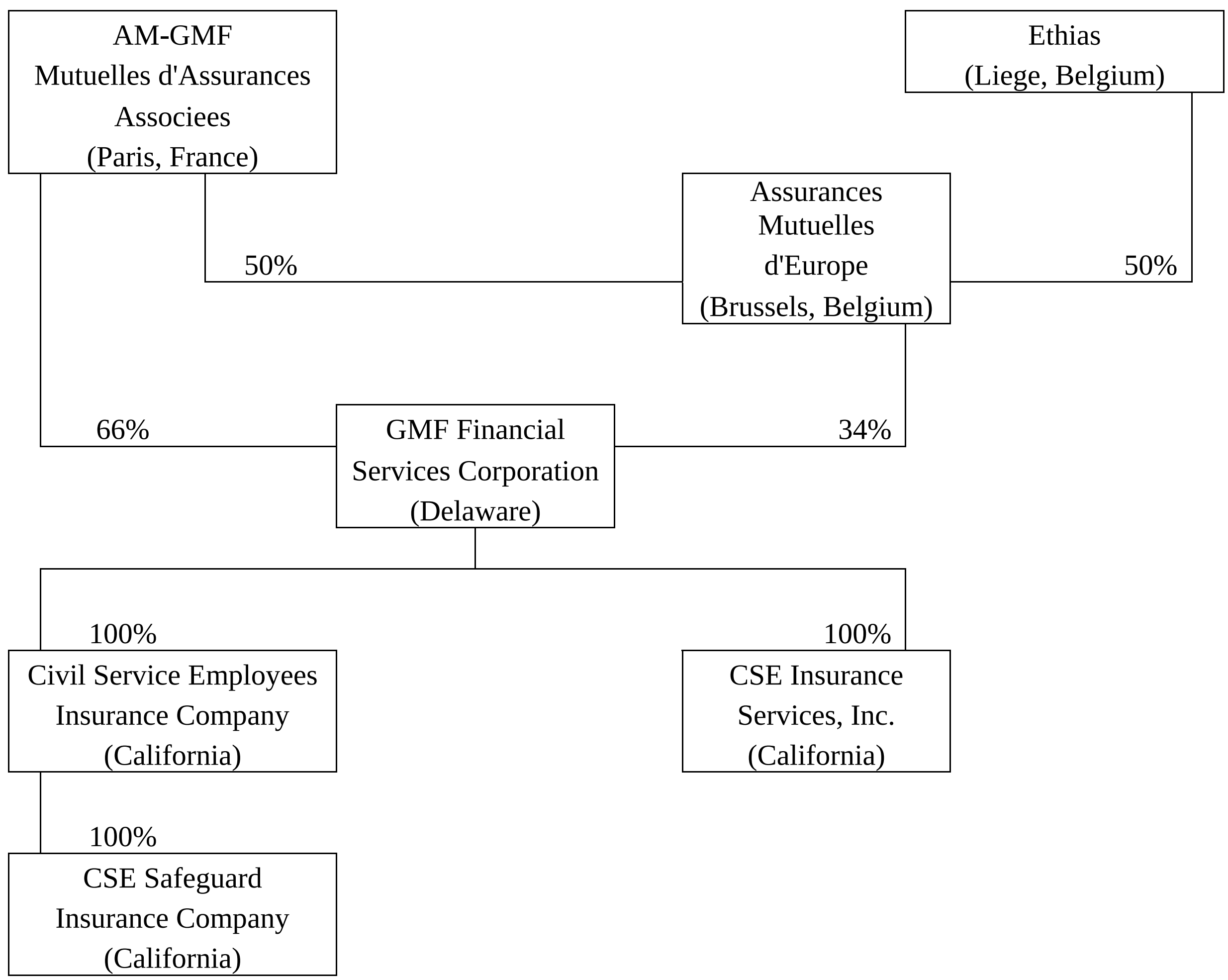
In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; and sales and advertising.

COMPANY HISTORY

The Company paid an extraordinary dividend of $6,631,000 to its parent company, Civil Service Employees Insurance Company in 2006. The dividend was approved by the California Department of Insurance pursuant to California Insurance Code Section 1215.5(g).

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system, of which AM-GMF Mutuelles d'Assurances Associees (AM-GMF) is the ultimate controlling entity. The following chart depicts the inter-relationship of the companies within the holding company system as of December 31, 2006:



Management of the Company is vested in an eight-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2006 follows:

Directors

Name and Residence	Principal Business Affiliation
Jaaq Baerten Tongeren, Belgium	Deputy Director General Ethias
Dirk van Berlaer Brussels, Belgium	Director and Actuary Ethias
Sophie Beuvaden Paris, France	Executive Vice President, Finance Covea

Directors

Name and Residence	Principal Business Affiliation
Pierre Bize Danville, California	Director, President and CEO Civil Service Employees Insurance Company
Jean Fleury Paris, France	Executive Vice President and General Secretary Covea
Véronique Florin ([1]) Paris, France	Project Manager, International Operations Covea
Patrice Forget La Celle-Saint-Cloud, France	Executive Vice President GMF Group
Richard J. Miles San Francisco, California	Retired Executive Vice President, Claims Civil Service Employees Insurance Company

Principal Officers

Name	Title
Pierre Bize	President
Gregory J. Parini	Secretary
Gardner J. Gray, Jr.	Senior Vice President and Chief Financial Officer
John C. Adiletti	Senior Vice President, Marketing
Frank V. Querques	Senior Vice President, Insurance Operations
David A. Brinker	Senior Vice President, Products and Support
Kai Y. Fung	Vice President, Actuarial
F. Lee Baumgartner	Vice President, Information and Technology
Robert M. Adams	Vice President, Internal Audit
James E. Williamson	Vice President, Claims

[1] Replaced in 2007 by Dominique Salvy

Inter-Company Agreements

Tax Allocation Agreement: The Company files federal income taxes on a consolidated basis with GMF Financial Services Corporation (GMFF) and other affiliates. The Company was party to a federal income tax agreement with GMFF effective January 1, 1990. Pursuant to this agreement, GMFF paid all of the Company's federal income tax obligations and in return the Company relinquished its claim to any tax refunds. The Company's immediate parent, Civil Service Employees Insurance Company (CSE), had an identical federal income tax sharing agreement with GMFF. On August 17, 2001, the Company received approval from the California Department of Insurance (CDI) to report federal income tax transactions based on the aforementioned agreement. The Company has requested and was granted a permitted accounting practice for this arrangement.

Cost Sharing Agreements: Pursuant to a cost sharing agreement, the Company received certain insurance-related services from CSE on a cost reimbursement basis. Services included agency appointments, policy rate and form development, reinsurance, premium collection, and claims settlement. The agreement dated back to January 1, 1996 and has been renewed a number of times since then. The current agreement was effective October 1, 2002 and expired on September 30, 2005.

Review of the cost sharing agreement indicated that, although an extension was approved by the Company's board of directors and the Company and CSE continued to operate under the terms of the agreement, the agreement had not been signed by the parties, nor had it been amended to reflect the extension date. A similar comment was made in the last examination report. It is recommended that the Company file this cost sharing agreement with the CDI as required by California Insurance Code Section 1215.5(b)(4), as no filing has ever been made.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2006, the Company was licensed to write various lines of property and casualty insurance in the following states:

Arizona	Nevada
California	Oregon
Colorado	Utah
Idaho	Washington

Direct premiums written by the Company in 2006 was $36.2 million in the following primary lines of business: homeowners multiple peril (41.1%), private passenger auto liability (29.8%), auto physical damage (20.3%), and fire, allied lines and all other (8.8%). The Company's target market was civil servants, but it sold to the general public as well. Territories in which premiums were written were California (59.8%), Utah (30.4%), Arizona (8.1%), Nevada (1.3%), and the remaining states (0.4%). Policies are marketed through approximately 500 independent agents located mostly in California, and two managing general agents, one located in Utah and the other in California. The Company wrote some earthquake policies, which were 100% reinsured with Lloyd's.

Managing General Agency Agreement - United Underwriters, Inc.

The Company entered into a managing general agency agreement with United Underwriters, Inc. (UU), of Provo, Utah effective June 6, 2005. Under the agreement, UU provided marketing, underwriting, premium collection and billing, policy processing, binding authority, and claims settlement for business produced in Utah. UU produced $9.2 million of direct written premium for the Company in 2006. The Company's transactions with UU are subject to the Managing General Agents (MGA) Act as defined by California Insurance Code Section (CICS) 769.81. CICS 769.82(b) requires that all MGAs for a domestic carrier be licensed as an agent in California, even though they are only producing in another state. CICS 769.83 requires certain minimum provisions be included in the MGA contract. A review of the managing general agency agreement with UU disclosed that several items were not addressed in the contract. Items specifically missing included, but are not limited to:

1) Records of the MGA shall be in a form usable to the commissioner. 769.83(d)
2) All claims shall be reported to the insurer in a timely manner. 769.83(g)(1)
3) That upon an order of liquidation of the insurer all claim files shall become the sole property of the insurer or its estate. (769.83(g)(3)
4) The timely transmission of electronic claim files. 769.83(h)

It is recommended that the Company comply with CICS 769.82(b) by having UU obtain a California broker-agent license. It is also recommended that the Company comply with CICS 769.83 by amending the MGA agreement to include all applicable provisions.

General Agency Agreement – Alliance United Insurance Services, Inc.

The Company had a managing general agency agreement with Alliance United Insurance Services, Inc. (AUIS), a California licensed agent. Under the agreement, AUIS provided marketing, underwriting, premium collection and billing, policy processing, and binding authority for business produced in California. AUIS produced $5.8 million of direct written premium for the Company in 2006. The Company terminated the agreement in 2006.

REINSURANCE

Pooling Agreement

The Company has been party to a reinsurance pooling agreement with its parent company, Civil Service Employees Insurance Company (CSE) since January 1, 1990. The reinsurance pooling agreement was last amended January 1, 2006. The agreement provides for the pooling and distribution of premiums, losses, loss adjustment and underwriting expenses. Under the terms of the agreement, the Company cedes 100% of its net writings (after non-affiliated reinsurance) to CSE which in turn retrocedes 33.33% of the combined net writings of both companies to the Company. It is recommend this agreement be filed with the California Insurance Department pursuant to California Insurance Code Section (CICS) 1215.5(b)(4), since amendments were made to the agreement and no filing has ever been made.

Assumed

The only business the Company assumed was from the reinsurance pooling agreement described above.

Ceded

The Company was covered under the following multiple layers of excess of loss and quota share contracts at December 31, 2006:

Type of Contract	**Reinsurers**	**Company Retention**	**Reinsurer's Maximum Limits**
Property Excess of Loss	Authorized, Approved or Accredited: Employers Mutual Casualty Company – 3.0% Motors Insurance Corporation – 50.0% Hannover Ruckversicherungs-Aktiengesellschaft – 10.0% Partner Reinsurance Company of the U.S. – 20.0% The Toa Reinsurance Company of America – 12.5% Unauthorized: Shelter Mutual Insurance Company – 4.5%	$ 400,000 per risk $1.0 million per occurrence	$ 3.6 million per risk $ 4.0 million per occurrence
Property Treaty Excess of Loss	Various Lloyd's Syndicates – (Approved)	$ 4.0 million	$ 6.0 million
Property Facultative Excess of Loss	Munich American Reassurance Company – (Authorized)	$ 10.0 million	$ 25.0 million

Type of Contract	**Reinsurers**	**Company Retention**	**Reinsurer's Maximum Limits**
Casualty Excess of Loss	All Authorized: GE Reinsurance Corporation – 32.5% Motors Insurance Corporation – 35.0% Partner Reinsurance Company of the U.S. – 20.0% The Toa Reinsurance Company of America – 12.5%	$ 300,000 per event $ 1.0 million per event for ECO/XPL	$ 700,000 per event $ 5.0 million per event for ECO/XPL
Personal Umbrella Liability Quota Share	Munich American Reassurance Company – (Authorized)	5% of $ 1.0 million	95% of $ 1.0 million and 100% over $ 1.0 to $ 5.0 million
Commercial Umbrella Liability Quota share	Munich American Reassurance Company – (Authorized)	5% of $ 1.0 million	95% of $ 1.0 million and 100% over $ 1.0 to $ 5.0 million
Catastrophe Excess of Loss	Various Authorized (A) and Unauthorized (U) Reinsurers:		
	First Layer A - 47.0% , U - 48.0%, Total - 95.0%	$ 5.0 million	$ 5.0 million
	Second Layer A - 46.5%, U - 48.5%, Total - 95.0%	$ 10.0 million	$ 7.5 million
	Third Layer A - 38.0%, U - 57.0%, Total - 95.0%	$ 17.5 million	$ 12.5 million
	Fourth Layer A - 43.0%, U - 52.0%, Total - 95.0%	$ 30.0 million	$ 20.0 million
	Fifth Layer A - 48.0%, U - 52.0%, Total - 100.0%	$ 50.0 million	$ 25.0 million
	Sixth Layer A - 59.5%, U - 40.5%, Total - 100.0%	$ 75.0 million	$ 25.0 million

After review of the reinsurance contracts listed above, it was noted that the contracts with Munich American Reassurance Company had insolvency clauses that did not comply with CICS 922.2. The Company has already taken action to amend the contracts. Aside from the pooling agreement, total recoverable on paid and unpaid losses at December 31, 2006 was $508,000 and $2.7 million, respectively.

ACCOUNTS AND RECORDS

The examination included a review of the Company's general controls over its information systems. A number of weaknesses were noted in areas such as security and access controls, physical security, program change controls, and business continuity planning. The noted weaknesses were presented to the Company along with recommendations to strengthen its controls. It was noted that many of the specific findings from the prior examination continue to exist and have not been addressed. The Company's response to many of the unaddressed findings has been that it will take it under advisement. The Company should evaluate the recommendations and make appropriate changes to strengthen its information system controls.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2006

Underwriting and Investment Exhibit for the Year Ended December 31, 2006

Reconciliation of Surplus as Regards Policyholders from December 31, 2002 through December 31, 2006

Statement of Financial Condition
as of December 31, 2006

Assets	Ledger and Nonledger Assets	Nonadmitted Assets	Net Admitted Assets	Notes
Bonds	$ 37,823,569	$	$ 37,823,569	
Cash and short-term investments	28,821,561		28,821,561	(1)
Investment income due and accrued	470,441		470,441	
Uncollected premiums and agents' balances in the course of collection	1,022,864	499,533	523,331	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	3,700,967		3,700,967	
Amounts recoverable from reinsurers	197,480		197,480	
Aggregate write-ins for other than invested assets	201,072	201,072		
Total assets	$ 72,237,954	$ 700,605	$ 71,537,349	

Liabilities, Surplus and Other Funds			
Losses		$ 16,417,374	(2)
Loss adjustment expenses		6,845,944	(2)
Commissions payable, contingent commissions and other similar charges		965,423	
Other expenses (excluding taxes, licenses and fees)		896,249	
Taxes, licenses and fees (excluding federal and foreign income taxes)		79,197	(3)
Unearned premiums		17,219,626	
Advance premiums		290,003	
Payable to parent, subsidiaries and affiliates		4,525,595	
Aggregate write-ins for liabilities		531,928	
Total liabilities		47,771,339	
Common capital stock	$ 3,400,000		
Gross paid-in and contributed surplus	11,660,000		
Unassigned funds (surplus)	8,706,010		
Surplus as regards policyholders		23,766,010	
Total liabilities, surplus and other funds		$ 71,537,349	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2006

Statement of Income

Underwriting Income		
Premiums earned		$ 37,204,737
Deductions:		
Losses incurred	$ 15,212,516	
Loss expenses incurred	5,474,533	
Other underwriting expenses incurred	13,782,100	
Total underwriting deductions		34,469,149
Net underwriting gain		2,735,588
Investment Income		
Net investment income earned	$ 2,616,290	
Net realized capital loss	(355,269)	
Net investment gain		2,261,021
Other Income		
Net loss from agents' or premium balances charged off	$ (52,759)	
Finance and service charges not included in premiums	273,432	
Aggregate write-ins for miscellaneous income	29,648	
Total other income		250,321
Net income before federal income taxes		5,246,930
Federal income taxes incurred		0
Net income		$ 5,246,930

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2005		$ 25,664,311
Net income	$ 5,246,930	
Change in nonadmitted assets	(164,631)	
Dividends to stockholders	(6,631,000)	
Aggregate write-ins for losses in surplus	(349,600)	
Change in surplus as regards policyholders for the year		(1,898,301)
Surplus as regards policyholders, December 31, 2006		$ 23,766,010

Reconciliation of Surplus as Regards Policyholders
from December 31, 2002 through December 31, 2006

	Gain in Surplus	Loss in Surplus	
Surplus as regards policyholders, December 31, 2002, per Examination			$ 16,343,638
Net income	$ 12,277,421	$	
Change in net unrealized capital losses		27,974	
Change in nonadmitted assets		677,475	
Change in provision for reinsurance	2,831,000		
Dividend to stockholder		6,631,000	
Aggregate write-ins for losses in surplus		349,600	
Total gains and losses	$ 15,108,421	$ 7,686,049	
Net increase in surplus as regards policyholders			7,422,372
Surplus as regards policyholders, December 31, 2006, per Examination			$ 23,766,010

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Cash and Short-Term Investments

Although the majority of its investments were held in a qualified custodian as required by California Insurance Code Section (CICS) 1104.9, it was noted that the Company maintained a significant amount of cash and short-term investments at year end with banks which are no longer domiciled in California. In addition, CICS 1104.1 requires moneys and securities in excess of reasonable business needs to be maintained in California. It is recommended the Company deposit its cash and short-term investments with a qualified custodian, subcustodian, or depository located in California pursuant to CICS 1104.1 and 1104.9.

(2) Losses and Loss Adjustment Expenses

Based on an analysis by a Casualty Actuary for the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2006 were found to be reasonably stated and have been accepted for purposes of this examination.

(3) Taxes, Licenses and Fees

CICS 1872.8(a) states, in part, that each insurer doing business in the State of California must pay an annual Vehicle Fraud Assessment Fee for each vehicle insured under an insurance policy it issues in California. The fee provides funding for the increased investigation and prosecution of fraudulent automobile insurance claims and automobile theft in California. The review for the examination period from January 1, 2003 through December 31, 2006 indicated a total underpayment for the four-year period of $19,515.15.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Management and Control – Intercompany Agreements (Page 5): It is recommended that the Company file the cost sharing agreement with the California Department of Insurance (CDI) as required by California Insurance Code Section (CICS) 1215.5(b)(4).

Territory and Plan of Operation – Managing General Agency Agreement (Page 6): It is recommended that the Company comply with CICS 769.82(b) by having United Underwriters, Inc. obtain a California broker-agent license. It is also recommended that the Company comply with CICS 769.83 by amending the Managing General Agency agreement to include all applicable provisions.

Accounts and Records (Page 10): It was noted that many of the specific findings from the prior examination continue to exist and have not been addressed. It is recommended that the Company review the recommendations made regarding its information systems and make appropriate changes to strengthen internal controls.

Comments on Financial Statement Items – Cash and Short-Term Investments (Page 14): It is recommended the Company deposit its cash and short-term investments with a qualified custodian, subcustodian, or depository located in California pursuant to CICS 1104.1 and 1104.9.

Comments on Financial Statement Items – Taxes, Licenses and Fees (Page 14): The Company under reported the vehicle counts supporting the Vehicle Fraud Assessment Fee, as defined by CICS 1872.8. Total underpayment of the Vehicle Fraud Assessment Fee for the four-year period was $ 19,515.15. It is recommended the Company submit revised filings for this period.

Previous Report of Examination

Management and Control – Intercompany Agreements (Page 6): It was recommended that the Company renew all inter-company agreements prior to their expiration. The Company complied by extending the cost sharing agreement to September 30, 2005, but it was allowed to expire and was never signed by the parties. It was noted that the Company's board of directors approved extension of the agreement until December 2007, but the agreement was not revised. Although not recommended in the prior examination, it is now recommended that the Company file the cost sharing agreement with the CDI pursuant to CICS 1215.5(b)(4).

Management and Control – Conflict of Interest (Page 7): It was recommended that the Company retain a completed set of conflict of interest statements for review at any time. The Company has complied with this recommendation.

Corporate Records (Page 7): It was recommended that the Company comply with CICS 1201 regarding approval of investments by the board of directors. The Company has complied with this recommendation.

Territory and Plan of Operation (Page 8): It was reported that Four Corners operated like a managing general agent although it did not handle claims for business it produced for the Company. The Company terminated its agreement with Four Corners in February, 2003.

Territory and Plan of Operation (Page 9): It was recommended that the Company execute an agreement with an entity before accepting any services in the future. The Company has complied with this recommendation.

Accounts and Records – Alliance United Insurance Services, Inc. (Alliance United) (Page 13): It was recommended that the Company request Alliance United to provide policy detail information to support the premium collected on behalf of the Company. The Company terminated its agreement with Alliance United in 2006.

Accounts and Records – Information System Controls (Page 13): It was recommended that the Company review its information system controls and address the control weaknesses noted in areas such as information security, program change control, physical security, disaster recovery and business continuity planning. Many of the specific findings from the prior examination continue to exist and have not been addressed. The Company's response to many of the unaddressed findings has been that it will take it under advisement.

Comments on Financial Statement Items – Losses and Loss Adjustment Expenses (Page 19): It was recommended that the Company immediately terminate certain described claims practices and institute controls and supervisory reviews over the claims operation. The Company has complied with this recommendation.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the officers and employees of CSE Safeguard Insurance Company during the course of this examination is gratefully acknowledged.

Respectfully submitted,

/S/

Isabel Spiker, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California